

No. 15,796

United States Court of Appeals
For the Ninth Circuit

G. A. MILLER, W. W. LORD, RALPH SMEED,
L. H. STAUS and JACK SMEED, Trustees
of John W. Smeed Estate,

Appellants,

vs.

SAM WAHYOU, DIAMOND-S RANCH CO., SAM
WAHYOU, K. R. NUTTING and THOMAS G.
LEE, as Trustees for the assets of Dia-
mond-S Ranch Co., THOMAS G. LEE, TOY
QUONG, JOE SIN, K. R. NUTTING, YIP K.
TOON and HERBERT JANG,

Appellees.

Appeal from the United States District Court
for the District of Nevada.

APPELLANTS' BRIEF.

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APPELLANTS' BRIEF.

I.

STATEMENT OF JURISDICTION.

Appellants, G. A. Miller, W. W. Lord, Ralph Smeed, L. H. Staus, and Jack Smeed, Trustees of John W. Smeed Estate, commenced this action as plaintiffs against A. E. Corbari and Marie Corbari, husband and wife, Sam Wahyou, Diamond-S Ranch

Co., a Nevada corporation, and K. R. Nutting, Thomas G. Lee, Sam Wahyou, and A. E. Corbari, as trustees for said corporation, asking for a money judgment against the defendants A. E. and Marie Corbari, praying that the assets of the defendant Diamond-S Ranch Co. be impressed with an equitable lien in favor of plaintiffs to secure the moneys alleged to be owed plaintiffs by the defendants A. E. and Marie Corbari, and, alternatively, for a money judgment against the defendant Sam Wahyou for the full amount of any money found due and owing plaintiffs from the defendants A. E. and Marie Corbari, including interest, attorneys' fees and costs. Thereafter, on October 21, 1954, plaintiffs filed an amended complaint (1T 25)¹ against Archie E. Corbari, Marie Corbari, Sam Wahyou, Diamond-S Ranch Co., a corporation, Forrest E. Macomber, A. E. Corbari, Sam Wahyou, K. R. Nutting, and Thomas G. Lee, as trustees for the assets of the Diamond-S Ranch Co., Thomas G. Lee, Toy Quong, Joe Sin, K. R. Nutting, Yip K. Toon, Herbert Jang, otherwise known as Herbert Jong, and D. W. Zignego. The relief demanded (1T 34, 35) consisted of a money judgment against the defendants Corbari, that a receiver be appointed to take over the assets of the Diamond-S Ranch Co., that plaintiffs be decreed a proportionate interests in the assets of the Diamond-S Ranch Co., for an accounting, that the defendants be enjoined

¹Page referrals to the transcript of record in Case No. 14,902, United States Court of Appeals for the Ninth Circuit, the initial appeal of this case, will be designated in the following manner, (1T); page referrals in Case No. 15,796 as, (2T).

from disposing of any of the assets of the Diamond-S Ranch Co., for an order directing that the property and assets of the Diamond-S Ranch Co. be sold and plaintiffs paid from the proceeds of the sale, and that plaintiffs have judgment against the defendants Wahyou, Macomber, Nutting, Lee, Quong, Sin, Toon and Jang (or Jong), and each of them, for payment of the obligation due and owing plaintiffs.

All defendants thereafter answered to the Amended Complaint (1T 41, 51, 57), but the action against the defendants D. W. Zignego and Forrest E. Macomber was dismissed by virtue of the pre-trial order of the District Judge dated January 18, 1955 (1T 130).

Both plaintiffs and defendants² filed motions for Summary Judgment. The District Court, on August 11, 1955 (1T 153), entered judgment in favor of plaintiffs as to the First Count of their amended complaint, against plaintiffs and in favor of defendants as to the Second, Third and Fourth Counts of the amended complaint, in favor of plaintiffs and against the defendants A. E. and Marie Corbari for costs, and in favor of all defendants except A. E. and Marie Corbari and against the plaintiffs, for the costs of those defendants. From this judgment plaintiffs appealed to this Court, and Notice of Appeal was filed on September 9, 1955 (1T 154).

The case having been argued and submitted and the Court being advised in the premises, on June 8,

²The parties will be referred to as plaintiffs and defendants in this brief.

1956, handed down its mandate, which mandate was in the following form (2T 3, 4, 5):

MANDATE

United States of America, ss:

The President of the United States of America
To the Honorable, the Judges of the United States
District Court for the District of Nevada,
Greeting

Whereas, lately in the United States District Court for the District of Nevada, before you or some of you, in a cause between G. A. Miller, et al., plaintiffs and Archie E. Corbari, etc., et al., defendants, No. 1029, a judgment was duly filed and entered on the 11th day of August, 1955, which said judgment is of record and fully set out in said cause in the office of the clerk of the said District Court, to which record reference is hereby made and the same is hereby expressly made a part hereof.

And Whereas, the said G. A. Miller, et al., appealed to this Court as by the inspection of the transcript of the record of the said District Court, which was brought into the United States Court of Appeals for the Ninth Circuit by virtue of an appeal agreeably to the Act of Congress, in such cases made and provided, fully and at large appears.

And Whereas, on the 25th day of April, in the year of our Lord, one thousand nine hundred and fifty-six, the said cause came on to be heard from the said United States Court of Appeals for the Ninth Circuit, on the said transcript of record, and was duly submitted:

On Consideration Whereof, it is now here ordered and adjudged by this Court, that the judgment of the said District Court in this cause be, and hereby is reversed and that this cause be, and hereby is remanded to the said District Court for a finding as to whether Wahyou has sustained such a burden of proof on the basis of the evidence presently in the record or any additional evidence the parties may offer with costs in this Court in favor of the appellants and against the appellees.

It is further ordered and adjudged by this Court that the appellants recover against the appellees for their costs herein expended and have execution therefor.

You, Therefore, Are Hereby Commanded that such proceedings be had in said cause, in conformity with the opinion and judgment of this Court, as according to right and justice, and the laws of the United States, ought to be had, the said appeal notwithstanding.

Witness the Honorable Earl Warren, Chief Justice of the United States, the twenty-third day of July, in the year of our Lord one thousand nine hundred and fifty-six.

(June 8, 1956.)

/s/ Paul P. O'Brien,
Clerk, United States Court of
Appeals for the Ninth Circuit.

Costs: Clerk \$25.00, Printing record \$413.87,
Total \$438.87.

(Endorsed): Filed August 6, 1956.

The case then came on regularly for trial before the Hon. John R. Ross, Judge of the District Court for the District of Nevada, on June 4, 1957, before the Court without a jury, for the purpose of taking evidence upon the issue specified in the mandate of the United States Court of Appeals for the Ninth Circuit, No. 14902, and entered on the 23rd day of July, 1956. The Court, after hearing the witnesses and considering the evidence as introduced, concluded as a matter of law as follows (2T 16, 17):

“1. That Plaintiffs are entitled to the judgment against the Defendants Archie E. Corbari, otherwise known as A. E. Corbari, and Marie Corbari, his wife, as heretofore determined by this Court in the Order granting Summary Judgment made and filed herein on August 11, 1955.

2. That Plaintiffs are entitled to take nothing against the Defendants Sam Wahyou, Diamond-S Ranch Co., a Nevada Corporation, Thomas G. Lee, Toy Quong, Joe Sin, K. R. Nutting, Yip K. Toon and Herbert Jang, otherwise known as Herbert Jong, and that the said Defendants are entitled to their costs of Court herein incurred.

Dated: September 20, 1957

Filed: September 20, 1957

John R. Ross
United States District Judge”

Plaintiffs are citizens of the State of Idaho. The defendants A. E. and Marie Corbari are citizens of the State of Nevada. The defendant Sam Wahyou, individually and as trustee, is a citizen of the State of California. The Diamond-S Ranch Co. was in-

incorporated under the laws of the State of Nevada with its principal place of business at Galconda, Nevada, and if it exists at all is a citizen of the State of Nevada. The defendants Nutting and Lee, individually and as trustees, are citizens of the State of California. The defendant Macomber is a citizen of the State of California. The defendants Quong, Sin, Toon, Jang (or Jong), and Zignego are citizens of the State of California.

The amount here in controversy, exclusive of interest and costs, exceeds the sum of Three Thousand Dollars (\$3,000.00).

The District Court's jurisdiction in the action was based on Title 28, U.S.C.A., Sections 1332 and 1655. This Court has jurisdiction to determine this appeal under Title 28, U.S.C.A., Section 1291, and Rule 73, Federal Rules of Civil Procedure.

II.

STATEMENT OF THE CASE.

The facts in this case show that on or about December 31, 1948, the defendants A. E. Corbari and Marie Corbari made, executed and delivered to plaintiffs' decedent their promissory note in the amount of \$15,041.34 (1T 8), which amount with interest, except a payment of \$750.00 remains due, owing and unpaid (1T 146).

Thereafter on or about the 22nd day of February, 1950, A. E. Corbari agreed with the plaintiffs that he

would assign to plaintiffs as security for the payment of said note all of his interest in the Diamond-S Ranch Company, in which he owned 310 of 1572½ shares outstanding (1T 69). Following this agreement to assign, specifically on the 7th day of September, 1950, the directors of the Diamond-S Ranch Company, with the aid of Forrest Macomber, their attorney, effected a voluntary dissolution of the Diamond-S Ranch Company under the laws of the State of Nevada (1T 72, and Pre-trial Exhibit No. 8, 1T 131). Thereafter, on October 31, 1950, A. E. Corbari and Marie Corbari executed formal assignment (1T 84, 85) of all their right, title and interest in and to the assets of the Diamond-S Ranch Company, then a dissolved corporation, to plaintiffs.

Following the voluntary dissolution of the Diamond-S Ranch Company on September 7, 1950, the directors of the company, trustees under the statutes of Nevada, did not wind up the affairs of the corporation and distribute the assets as required to do by the laws of Nevada. Instead, they operated the corporation exactly as theretofore and continued to do so until the charter was attempted to be revived in December, 1951 (1T 72), without recognizing any interest in Corbari or in these plaintiffs.

Other pertinent facts are that on January 4, 1949, Corbari delivered to the Bank of America his 310 shares of Stock in the Diamond-S Ranch Company, a Nevada corporation, endorsed in blank as security for the payment of an obligation to the Bank, and at the same time executed a general pledge agreement to

the Bank (1T 106, 107, 108). On September 18, 1950, this pledge agreement was replaced with a new pledge executed by Corbari to the Bank of America (1T 108 and Pre-trial Exhibit 2, 1T 130), to secure the obligation owing to the Bank of America covered by the first pledge, and to further secure obligations owing to one Zignego and attorney Macomber. This second pledge was executed subsequent to the agreement to assign to Smeed of February 22, 1950, and subsequent to the dissolution of the corporation. Thereafter, on October 17, 1950, the Bank of America sold to the defendant, Sam Wahyou, Corbari's note (1T 48, 70 and 126) and the September 18, 1950, pledge (1T 106), in consideration of the payment by Wahyou of the balance due on Corbari's note to the Bank in the amount of \$5,000.00, plus interest. On February 9, 1951, Forrest Macomber, acting as attorney for Corbari and at the same time being the legally retained counsel for the Diamond-S Ranch Co. and for Sam Wahyou personally, wrote plaintiffs, offering to settle the obligation due them and secured by the assignment, for the sum of \$5,000.00 (1T 99), which offer was rejected. On March 26, 1951, plaintiffs' assignment of October 31, 1950, was recorded among the land records of Humboldt County, Nevada, the county in which the real property assets of Diamond-S Ranch Co. are located (1T 12).

On May 14, 1951 (Pre-trial Exhibit No. 4, 1T 131), the defendant Sam Wahyou signed a notice of sale of the stock of the Diamond-S Ranch Co. previously held by Corbari, to take place on May 21, 1951, and

in that notice recited that the sale was for the purpose of foreclosing a July 10, 1950, pledge of Corbari to the Bank of America which Wahyou had acquired. It should be here noted that the pledge referred to in the notice of sale can only be the second pledge agreement dated September 18, 1950 (Pre-trial Exhibit No. 2, 1T 130), and it should be further noted in that agreement that the date of July 10, 1950, is the date of the note being secured by the pledge, whereas the date of September 18, 1950, is the actual date of the pledge.

On May 21, 1951, the sale of the stock was made to one Gordon J. Aulik, an associate of Forrest Macomber, acting for and on behalf of Sam Wahyou (1T 107; 2T 73). The sale was conducted by Forrest Macomber, the attorney for Sam Wahyou, Corbari, and the Diamond-S Ranch Co. (2T 72, 73). Plaintiffs received no notice of this sale.

Following all of the transactions hereinbefore set forth, on October 10, 1951, the stockholders of the Diamond-S Ranch Company executed Appointment of Agent to revive the corporation, appointing Wahyou, Nutting and Lee as such agents (Pre-trial Exhibit 9, 1T 131). This instrument recited that defendants Wahyou, Nutting, Lee, Jang, Quong, Sin and Toon were holders of all of the stock and that Wahyou owned 631 shares. It should be noted that at dissolution Wahyou owned 321 shares, the difference being the Corbari stock.

On October 10, 1951, said agents executed under oath a Certificate of Revival or Renewal (Pre-trial

Exhibit 9, 1T 131), in which it was stated that the corporation had been carrying on its business since the date of its dissolution. On December 7, 1951, the certificate was filed with the Secretary of State of the State of Nevada (Pre-trial Exhibit 9, 1T 131), and on April 4, 1952, the Secretary of State issued his certificate of renewal (Pre-trial Exhibit 9, 1T 131).

The case having been returned to the District Court for a determination of whether or not the defendant Wahyou had sustained his burden of proof, trial was had before the Hon. John R. Ross. At this hearing the proof was limited as to the value of the stock which Wahyou had purchased to determine whether or not the transaction was fair.



III.

SPECIFICATION OF ERRORS.

1. The Court erred in failing to grant plaintiffs' Motion for Judgment at the close of defendants' case for the reason that the defendant Wahyou failed to sustain the burden of proof as to the bona fides of the transaction.

2. The Court erred in failing to find that the transaction on the part of Wahyou is one which would enrich the said Wahyou.

3. The Court erred in failing to find that the sale of the Corbari stock to Wahyou was void because Wahyou had made misuse of his office as Trustee.

4. The Court erred in failing to find that Wahyou stood in the shoes of the Bank of America as Pledgee when he foreclosed and purchased Corbari's stock, and as such he violated his fiduciary duty to Corbari, his Pledgor, by purchasing the stock for a grossly inadequate price.

5. The Court erred in failing to find that the Corbari stock was worth substantially more than the price paid by Wahyou and that as a result Wahyou unjustly enriched himself.

6. The Court erred in failing to find that Wahyou at the time he made the purchase of the Corbari stock intended and believed that he was purchasing stock of a substantially greater value than the price paid.

7. The Court erred in making and entering its Finding of Fact No. 14, such Finding of Fact being against the weight of evidence and in conflict with the admitted facts and is clearly erroneous.

8. The Court erred in making and entering its Findings of Fact No. 16 in that each statement of fact contained therein is erroneous and contrary to the evidence and that the evidence clearly showed the Corbari stock to have substantial value.

9. The Court erred in making and entering its Findings of Fact No. 17 in that each statement of fact therein contained is erroneous and contrary to the evidence and that the evidence clearly showed the Corbari stock to have substantial value.

10. The Court erred in making its Conclusion of Law No. 2.

11. The Court erred in entering the Judgment of September 27, 1957.

12. The Court erred in granting Judgment to the defendants on Counts 2, 3 and 4 of the Amended Complaint for the reason that the defendants failed to sustain their burden of proof.

13. The Findings of Fact and Conclusions of Law are contrary to the weight of evidence and are not supported by competent evidence.

IV.

ARGUMENT.

The principal proposition of law before the Court is simple and can be stated as follows:

I.

WHEN A TRUSTEE DEALS WITH THE BENEFICIARY'S INTEREST IN THE TRUST, THE BURDEN IS UPON THE TRUSTEE TO PROVE THAT THE TRANSACTION IS FAIR AND INVOLVED NO MISUSE OF HIS OFFICE.

The laws of California place a very high duty on the trustee. Applicable sections of the California Civil Code follow:

“Sec. 2224. One who gains a thing by * * * the violation of a trust is, unless he has some other and better right thereto, an involuntary trustee of the thing gained for the benefit of the person who would otherwise have had it.”

“Sec. 2228. Trustee’s obligation to good faith. In all matters connected with his trust, a trustee is bound to act in the highest good faith toward his beneficiary, and may not obtain any advantage therein over the latter by the slightest misrepresentation, concealment, threat, or adverse pressure of any kind.”

“Sec. 2231. Trustee’s influence not to be used for his advantage. A trustee may not use the influence which his position gives to him to obtain any advantage from his beneficiary.”

“Sec. 2233. To disclose adverse interest. If a trustee acquires any interest, or becomes charged with any duty, adverse to the interests of his beneficiary in the subject of the trust, he must immediately inform the latter thereof, and may be at once removed.”

“Sec. 2234. Trustee guilty of fraud, when. Every violation of the provisions of the preceding sections of this article is a fraud against the beneficiary of a trust.”

Section 2235 of the Civil Code of California provides:

“All transactions between a trustee and his beneficiary during the existence of the trust, or while the influence acquired by the trustee remains, by which he obtains any advantage from his beneficiary, are presumed to be entered into by the latter without sufficient consideration, and under undue influence.”

- A.** Where a trustee fails to prove that a transaction by which he acquires his beneficiaries' interest in the trust property was fair and equitable and without undue influence, the transaction will be set aside.

Entirely apart from the statute it is the universal rule of law that a fiduciary may not acquire his principal interest in trust property unless he deals openly, fairly and without undue influence. It is not an arms-length transaction.

3 Bogert, Trusts & Trustees 160, Section 493, expresses the rule thusly:

"Thus, if a trustee holds stock in trust and deserves to buy out the beneficiaries' interest, he should tell all he knows and believes about the present and probable future of the corporation whose stock he holds in trust, and, if he conceals information which he has that the corporation is about to be able to increase its profits greatly, he will not have performed his duty to the cestui, and the transaction will be voidable by the cestui. . . . Secondly, the Courts place upon the fiduciary who has received an advantage in a direct transaction with his principal the burden of showing that, if the arrangement purported to be one for a consideration, the consideration was adequate."

Winn v. Shugart, 112 F.2d 617 (CCA 10th 1940) enunciates the same rule. In that case a trustee purchased from his beneficiaries their interest in certain oil and gas property which was the corpus of the trust. Later the beneficiaries sued the trustee for an accounting and division of trust assets. The Court held that there was a complete absence of unfair dealing by the trustee, but announced the standard of

conduct to which a trustee must be held in the following language:

“It is necessary, therefore, only that we scrutinize the transaction of March 11, 1928, to ascertain if Shugart discharged that high degree of responsibility which the law placed upon a trustee, where he himself deals with the beneficiaries of the trust.

While transactions between a trustee and the cestui que trust are not prohibited, such transactions will be most severely scrutinized; a trustee may not profit by any transaction he may have in relation to the trust estate at the expense of the beneficiaries. In all his dealings with the trust estate he is held to the highest degree of candor and fairness. He must not only be strictly truthful in all his representation but must not remain silent concerning any matter of which he has knowledge that would throw light upon the trust estate. Courts of equity will set aside a transaction had by a trustee with the beneficiaries on the slightest ground. It would be needless to cite any authorities to sustain this statement. It is the unanimous holding of all Courts. It is in this light that the transaction must be viewed.”

When this case was returned to the Federal District Court of Nevada for hearing on whether or not the transaction complained of was fair and involved no misuse of the trustee's office, the burden of proof was placed upon the defendant Wahyou. The question before the Court is: Was that burden sustained? If that burden was not sustained, then the trial Court was in error in holding as it did, and judgment should

be entered for the plaintiff. It is well to remember that Wahyou was the trustee of the assets of a dissolved corporation and that the certificate of stock which he purchased from the bank had been pledged to the bank, not to him.

He stated in his first deposition that he purchased the stock from the bank because he thought it was worth more money than was owed on it, perhaps \$10,000.00 more (1T 112). Therefore, at the outset of this transaction, the purpose was stated by Wahyou, the trustee, that he intended to make money by purchasing the certificates. Thereafter, when the foreclosure took place, attorney Macomber, who represented Corbari, the Diamond-S Ranch Co. and Wahyou, made the arrangements for the sale, posted the notices and had his assistant, Aulit (2T 73) purchase the certificate of stock for Wahyou. The amount of the purchase price was the amount paid the bank for the pledge. It is interesting to note that there were no others at the sale and that there is no evidence that Corbari or Corbari's assignee Smeed had ever been notified of the time and place of the sale.

In reviewing the evidence as offered by the defendant Wahyou at the trial, there are two things to look for—proof to overcome the presumption of undue influence and proof to overcome the presumption of insufficient or lack of consideration.

The record is absolutely silent on lack of undue influence. The only proof as to the sale was that offered by Mr. Aulit, who simply testified as to the jurisdictional requirements having been met. There is no evi-

dence that Corbari was notified of the time, place or manner of sale. There was no evidence that Wahyou told Corbari that he believed the stock was worth more than he was going to pay for it and that he, Wahyou, would be able to gain back some of the money that Corbari owed him. On the other hand all of the evidence is that Wahyou's intentions were to make a profit for himself at the expense of his beneficiary.

From Wahyou's depositions of October 18, 1952 (1T 112), and October 20, 1956 (2T 158), it is perfectly obvious that Wahyou sincerely believed that the assets represented by the shares of stock which he bought was far in excess of the value that he paid for the certificate of stock. It is further obvious that he did not intend to credit Corbari's account or to give any of the profits to Corbari (2T 68, 69, 82, 83). Wahyou's intention to make a profit from this transaction as he has so eloquently stated in his two depositions and on direct examination is in the eyes of the law "unjust enrichment", and should void the sale.

Wahyou's entire course of conduct was one to gain for himself, from this transaction, money which would have gone to Corbari or Corbari's assignee had the transaction not taken place. Apparently every act and thing done to complete the transaction was done with this intention. If there was any intention to do anything for Corbari or Corbari's assignee, there is no evidence of that fact. The defendants, having rested without a scintilla of proof on this point, rested too soon and thereby encompassed their defeat.

B. A fiduciary acquiring his beneficiary's interest in trust property must pay fair and adequate consideration therefor.

In *Winn v. Shugart*, supra, the Court emphasized that:

“A trustee may not profit by any transaction he may have in relation to the trust estate at the expense of the beneficiaries.”

Thompson v. Afro-American Co., 185 F.2d 1014 (CCA 4th 1950) and *McDonald v. Hewlett*, 102 Cal. App. 2d 680, 228 P.2d 83, 24 ACR 2d 1281 (1951) are to the same effect.

This Court's opinion in *G. A. Miller, et al. v. Sam Wahyou, et al.*, 235 F.2d 612 (CCA 9th 1956) expressed the same view, where it was said:

“However, while a trustee may purchase his beneficiary's interest under the general law of trusts the trustee must carry the burden of proving that the transaction whereby he acquired the beneficiary's interest was fair and involved no misuse of his office.”

The *Thompson* and *McDonald* cases, supra, cited by this Court, establish that adequate consideration is one of the elements of fairness which the trustee is required to prove.

Let us view the evidence as submitted by the defendants in their attempt to meet this burden of proof. Their chief witness, of course, was Mr. Wahyou, and his testimony was replete with statements that he bought this stock for the purpose of making money and that he had no intention of crediting any overplus to Mr. Corbari or to the debt owed him by

Corbari. He also testified that they had offered the ranch for sale at prices ranging from \$150,000.00 to \$240,000.00 (2T 74, 75) and that in 1954 they offered it at a price close to a million dollars (2T 176-182). But the most interesting fact is that the corporation borrowed \$225,000.00 on this property in 1954 and that was on the real property alone. The deposition of Mr. Robert Wisecarver (2T 173) shows that Mr. Sam Wahyou requested the loan from the Central Valley Bank and that Mr. Wisecarver made the appraisal. The land was appraised at \$472,000.00 and the improvements at an additional \$14,300.00. The bank made a loan of \$225,000.00 with the ranch as security. Mr. Wisecarver also testified that the basis for loans on the part of the bank was 50% of the appraised value and that the value as fixed by Mr. Wisecarver was at that time to the best of his judgment a fair value of the property.

The book value of the land as shown by the comparative balance sheet was \$96,473.32 (Defendants' Exhibit No. 30B, 2T 25). If based on the Wisecarver appraisal, and certainly it was an impartial one, the real property was worth \$487,300.00, then the difference between the book value and the actual value of the real property was approximately \$400,000.00. A simple mathematical formula now may be applied to compute the actual value of the Corbari's stock. Corbari stock was 20% of the total outstanding, so for each one hundred thousand dollars of actual value of the corporation his certificate would represent a value of \$20,000.00. Therefore, if the market value of the

real estate was in excess of the book value, then for each one hundred thousand dollars of such additional value there would be an additional \$20,000.00 value to Corbari's stock. The book value of the land was \$96,472.42. Mr. Wisecarver appraised the property at \$487,300.00 or an additional value of \$381,000.00. This would give \$78,200.00 additional value to the Corbari certificate.

Mr. Charles Sewell qualified himself as an expert witness as to the value of real estate and with his knowledge of the property involved and the investigation he made of the property, testified as to a valuation of \$320,000.00 for the real estate (2T 96).

Mr. Harley McDowell, an appraiser, testified as to his inspection of the property and fixed the valuation at \$350,000.00 (Plaintiffs' Exhibit No. 3, 2T 25). Mr. Jack Utter, a real estate agent from Nevada, testified the value of the property was \$350,000.00 (2T 134).

Again reverting to our formula and the difference between the book value and the actual value of the property, the Corbari stock was worth, according to these appraisals, approximately \$50,000.00 as contrasted to the \$5,000.00 purchase price paid by Wahyou.

Even the testimony of the witness Hogue demonstrates that Wahyou paid a grossly inadequate price for the stock. In August of 1953 Mr. Frank Hogue testified (2T 41) that he had purchased one-third of the outstanding stock of this corporation from Mr. Wahyou and that he paid \$35,000.00 for the one-third

interest. This is in contrast to \$5,000.00 being paid for Mr. Corbari's 20%. The sale of the Corbari stock represented \$16.00 per share. The sale of the Wahyou stock to Hogue represented \$66.30 a share or a difference of \$50.00 per share. On that basis the Corbaris' stock had a value of \$15,500.00. This figure closely approximates Wahyou's estimate that he would make 10 or 15 thousand dollars out of the deal. It is further interesting to note that between the time of the sale of the Corbari certificate and the purchase of the Wahyou certificate by Hogue the corporation had lost \$400,000.00. This is shown by their comparative balance sheet (Exhibit B, 2T 25). The value of the one-third interest, had it been purchased on the comparative balance sheet figures of 1951 as compared with 1953, would have raised the value from \$35,000.00 to approximately \$135,000.00.

We further invite the Court's attention to the fact that every stockholder who testified at the hearing fixed the value of the land in excess of the book value. Mr. Nutting placed it at about \$60,000.00 more. Mr. Wahyou testified in his deposition that the property was worth \$150,000.00 to \$200,000.00 more than he paid for it (2T 162). The auditor, Mr. Buxton, testified that the value of the property on the books was cost (2T 64) and did not in any way reflect actual value. It is our position that if the property was worth any more than the book value, that value would have to be taken into consideration and being taken into consideration, it would raise the value of the certificate in excess of the amount Wahyou paid for

it. Wahyou did not have to buy this stock from the bank. He could have allowed the bank to sell the stock on foreclosure and he could have purchased it at the sale free and clear of any doubt as to the validity of the sale. However, he did not risk the bank selling the stock. Instead he purchased the pledge from the bank and conducted the sale himself. The very fact that he purchased the stock from the bank indicated that he had a plan in mind whereby he would acquire an advantage which he did not want to risk by letting the bank conduct the sale as the pledgee. The consideration paid by Wahyou for the stock was grossly inadequate and the sale should be voided.

II.

There is yet another reason why the transaction whereby Wahyou acquires the Corbari stock should be set aside.

A PLEDGE HOLDER IS IN A FIDUCIARY RELATIONSHIP WITH THE PLEDGOR AND MAY NOT PURCHASE THE PROPERTY OF THE PLEDGE UNLESS HE PAYS ADEQUATE CONSIDERATION THEREFOR.

It is the general rule of law, in the absence of a statute to the contrary, that a pledgee is incapacitated from becoming a bidder and purchasing the collateral held by him so as to free the property from the pledge and secure absolute title as against the pledgor (41 Am. Jur. 649; Pledge and Collateral Security, Section 90). This rule is considered in 3 Stanford Law Review 744 (1951) where the comment is:

“The well-established rule is that the pledgee may not obtain valid title to the property by purchasing at such a sale. The reason is clear. A pledgee owes a fiduciary duty to the pledgor to obtain the highest price reasonably possible on the sale. His own interest as a purchaser is to buy in the property as cheaply as possible. This conflict of interest and duty precludes a right to purchase the property.”

The pledge agreement here involved contains no reference to any right of the pledgee to purchase the subject matter of the pledge. Wahyou’s right to purchase stems solely from the California statute, California Civil Code, Section 3010, which reads as follows:

“Where property is sold at public auction, in the manner provided by Section three thousand and five of this Code, the pledgee or pledge holder may purchase said property at such sale.”

Wahyou, of course, stood in the shoes of the Bank of America, being charged with the same duties respecting the pledge as was the bank. 41 Am. Jur. 603, Pledge and Collateral Security, Section 67. His position was that of trustee of Corbari, the pledgor and Corbari’s assignees, these plaintiffs. *Ferro v. Citizens National Trust and Savings Bank*, 282 P.2d 849, 852 (Cal. 1955).

The Supreme Court of California had occasion to review a similar situation in the case of *Hudgen v. Chamberlain*, 120 Pac. 422 (Cal. 1911). In that case a debtor had pledged certain shares of stock to

creditor A and other shares of stock to creditor B. The pledge agreement in this case permitted sale at private or public auction with or without notice and gave the pledgee the right to purchase the pledged stock. Upon default of the debtors, the creditors and pledgees, acting in concert, placed a large block of stock on the market, creating a panic and forcing the price down from a fair market value of \$3.00 a share to a sudden low of \$2.00 a share. At that point they purchased the pledged stock, realizing their profit of approximately \$11,000.00. The Court held:

“It is, of course, well settled that a pledgee, under such contracts as are shown here, may sell the property pledged in satisfaction of the pledges and purchase the same at the sale thereof; the only requirement being that the sale shall be fair and bona fide . . .

“But we do not construe the complaints as alleging facts showing simply that the defendants, upon the default of the plaintiff, proceeded merely to exercise their legal rights to sell the stock in the then condition of the market, unaffected by any action on their part. On the contrary it appears from the allegations of the complaint that these defendants held their stock independently of each other, and each block of stock as a separate pledge for the payment of their individual notes, and they collusively agreed to jointly offer for sale the separate shares of stock pledged to each, with the sole purpose of thereby depreciating the value of the stock in the then existing market, thereby creating a panic, and as a result thereof lessening the value of the stock, so as to be able to purchase it at greatly reduced figures;

and that they did so. We think this clearly states a cause of action.”

English v. Culley, 259 P. 355 (Cal. App. 1927, hearing denied by Supreme Court October 31, 1927) was a case where a pledge holder bought the pledge for \$20,000 and subsequently sold it for a prearranged price of \$38,303.41. The Court held this to be a violation of the trust, saying:

“While this may generally be true, still the relation existing between parties to a transaction, where collateral security is placed in the hands of a pledgee as security for the payment of a debt with power of sale in the case of default, is in the nature of a trust. The responsibility of the pledgee to the pledgor is similar to that of a trustee; he holds the stock for specific purposes—namely, to return it to the pledgor in the event of payment of the indebtedness, or if sold by him either at public or private sale to so act that the sale will be fair and bona fide. The fact that the pledgee himself may become the purchaser, by reason of the Code provision, which was not permitted at common law, affords an additional reason why the pledgee is held to the utmost good faith in dealing with the pledged property. *Hudgens v. Chamberlain*, 161 Cal. 710, 120 P. 422.”

This general rule is further stated in 76 A. L. R. 705, 722 and the cases annotated therein:

“The validity and efficacy of a purchase of the subject of a pledge by the pledgee, under an agree-

ment authorizing the purchase, must be determined solely on facts of each case and all the attendant circumstances, and cannot be made the subject of a specific rule. It may be said, however, that the cases show that, regardless of how unlimited the power and authority of a pledgee to purchase the pledged property may be, he will be held to the strictest good faith in dealing with it, and will not be permitted wantonly to sacrifice it for his own benefit. His position is generally held to be that of a fiduciary, and the fact that the power to purchase is conferred on him will not relieve him of his duties as a trustee to sell. Though mere inadequacy of the price at which the subject of the pledge was purchased does not of itself show lack of good faith or due care, and though no notice of the sale need be given to the pledgor or the public when the pledge agreement waives such requirement, yet such circumstances, when weighed together with other facts which indicate that the pledgee is not attempting to realize the amount of the debt by the sale, but is merely attempting to secure for himself the full title to the property at the lowest possible price, are generally held to show a dealing with the property incompatible with the pledgee's fiduciary character, which will warrant the Court in holding the sale and purchase invalid."

We therefore urge that this sale should be voided, because Wahyou violated his fiduciary position as a pledgee in knowingly purchasing the stock for many times less than its fair and true value.



Appendix.

Appendix

(EXHIBITS)

Page referrals to the transcript of record in Case No. 14,902, United States Court of Appeals for the Ninth Circuit, the initial appeal of this case, will be designated in the columns in the following manner, 1T; page referrals in the transcript in Case No. 15,796 as, 2T

Exhibit 1	1T 130
Exhibit 2	1T 130
Exhibit 3	1T 131
Exhibit 4	1T 131
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Exhibit A	2T 33
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Exhibit F	2T 53
Exhibit G	2T 86